

This letter concerns sales of tangible personal property used in the construction or maintenance of a community water supply. See 35 ILCS 105/3-5(34) and 35 ILCS 120/2-5(39). (This is a GIL.)

August 12, 2008

Dear Xxxxx:

This letter is in response to your letter dated January 29, 2008, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

This firm represents the ASSOCIATION. The Association is located in unincorporated COUNTY and supplies potable drinking water to its residents, along with a sanitary sewer which employs a spray irrigation system. Both of these systems come under the regulatory purview of the Illinois Pollution Control Board as well as the Illinois Environmental Protection Agency. Essentially, the Homeowners Association provides municipal utilities to its member residents in addition to several homes outside the Association boundaries. Our permit is attached hereto and incorporated by reference as Exhibit A.

Pursuant to the aforementioned regulations, the Association was forced to perform upgrades to its community water supply in that the levels exceeded federal standards for radium. As the Department is perhaps aware, radium standards in drinking water are promulgated by the United States Environmental Protection Agency pursuant to the Clear Water Act. The Illinois Pollution Control Board has adopted those regulations as identical-in-substance and the Illinois Environmental Protection Agency enforces those standards. As such, the Association was notified by the IEPA that it had to perform upgrades in order to meet these radium standards.

The Association began this process in 2005 and in 2006 it obtained permits from the IEPA. The bidding process began and in 2007, ABC was awarded the contract. Some work was performed in 2007, but the project is not yet complete. The project was

authorized in July of 2007. In December of 2007, ABC delivered the products to the site. It is anticipated that the upgrades will be completed within the next two months. The payment schedule and contract are attached hereto and incorporated by reference as Exhibit B. Within the last month or so, the Association was notified by ABC that unless the contractor was provided with a sales tax exemption number, it would be forced to charge the Association \$18,468.75. As a result, the Association filed for a sales tax exemption number, and that petition was denied by the Illinois Department of Revenue.

However, the denial noted that the Association could re-petition for relief. In doing the research and speaking with representatives of the Department, it was advised that an appeal could be taken before the Board of Appeals. Of equal importance, the Association discovered that effective January 1, 2008, the Department's informational bulletin (FY 2008-07, pg 2) noted that construction and maintenance of a community water supply is exempt from sales and use taxes. The Association meets the definition of a community water supply in that it serves approximately 220 homes. The informational bulletin ends by stating that 'the purchaser will need to provide a copy of the permit from the Environmental Protection Agency in order to make these tax-free purchases'.

This informational bulletin raises a number of questions which Department personnel have been unable to definitively answer. First and foremost, does this exempt an Association from sales tax on an entire project which straddles the effective date? Moreover, how is [sic] a contractor or a provider of these materials protect itself from a sales tax audit? In other words, is the IEPA permit tantamount to a partial sales tax number?

In any event, the main question is whether the ASSOCIATION remains exempt for its entire community water supply project despite the fact that construction commenced in December of 2007. Initially, Department personnel advised the Association to petition to the Board of Appeals. However, upon review of the application, representatives from the Department of Revenue subsequently suggested that this letter be tendered to its legal department for a letter ruling or its equivalent. It is in this context which this letter s drafted.

Clearly, the Department has recognized a legitimate sales tax exemption and has enacted the same as it relates to sales tax for community water supplies. What the Association is providing is tantamount to utility services. Any municipal [sic] providing this service would, of course, be exempt from sales tax. Accordingly, the Association respectfully requests that the Department exempt it from any sales tax with respect to its construction of upgrades to its community water supply system. Further, we respectfully request that said exemption be reduced to writing so we can formally advise our contractor.

In the event the Department has any questions, I would welcome the opportunity to discuss the matter in greater detail.

DEPARTMENT'S RESPONSE:

A contract to incorporate tangible personal property into real property is considered a construction contract. The term "construction contractor" includes general contractors, subcontractors, and specialized contractors such as landscape contractors. The tax liabilities

regarding construction contractors in Illinois may be found at 86 Ill. Adm. Code 130.1940 and 130.2075 on the Department's Internet website.

In Illinois, construction contractors are deemed end users of tangible personal property purchased for incorporation into real property. As end users of such tangible personal property, contractors incur Use Tax liability for such purchases based upon their cost price of the tangible personal property. See 86 Ill. Adm. Code 130.1940 and 86 Ill. Adm. Code 130.2075. Therefore, any tangible personal property that a construction contractor purchases that will be permanently affixed to or incorporated into real property in this State will be subject to Use Tax.

If a contractor does not pay the Use Tax liability to its suppliers, the contractors must self assess Use Tax liability and pay it directly to the Department. If the contractor has already paid a tax in another state regarding the purchase or use of such property, it will be entitled to a credit against its Illinois Use Tax liability to the extent that it has paid tax that was properly due to another state. See 86 Ill. Adm. Code 150.310. The Illinois Use Tax rate incurred by an out-of-State construction contractor on purchases of materials from an unregistered supplier located outside of this State is generally 6.25% as described in subsection (c) of Section 130.2075.

It is important to note that since construction contractors are the end users of the materials that they permanently affix to real estate, their customers incur no Use Tax liability, and the construction contractors have no legal authority to collect the Use Tax from their customers. However, many construction contractors pass on the amount of their Use Tax liabilities to customers in the form of higher prices or by including provisions in their contracts that require customers to "reimburse" the construction contractor for his or her tax liability. Please note that this reimbursement cannot be billed to a customer as "sales tax," but can be listed on a bill as a reimbursement of tax. The choice of whether a construction contractor requires a tax reimbursement from the customer or merely raises his or her price is a business decision on the construction contractor's part.

The Department's regulations state that when something that has been exempted becomes taxable as to sales that are made on or after some particular date, the date of sale will be deemed to be the date of delivery of the property. This is true even if such delivery is made under a contract that was entered into before the effective date of the new tax. The reverse is true when applied to something taxable, which later becomes exempt. See 86 Ill. Adm. Code 130.101(c). Since a construction contractor is deemed the end user of the tangible personal property, the delivery date to the construction contractor is the relevant date for purposes of Section 130.101(c).

Beginning January 1, 2008, sales of tangible personal property used in the construction or maintenance of a community water supply, as defined under 415 ILCS 5/3.145, that is operated by a not-for-profit corporation that holds a valid water supply permit under Title IV of the Environmental Protection Act are exempt from Use Tax Act, the Service Use Tax Act, the Service Occupation Tax Act and Retailers' Occupation Tax Act. 35 ILCS 105/3-5(34), 35 ILCS 110/3-5(26), 35 ILCS 115/3-5(27) and 35 ILCS 120/2-5(39). To document the exemption, qualifying not-for-profit corporations purchasing tangible personal property to be used in the construction or maintenance of a community water supply should give their suppliers a certificate that certifies that 1) it is a not-for-profit corporation; 2) it operates a community water supply as defined under Section 3.145 of the Environmental Protection Act; 3) it holds a valid water supply permit issued to it under Title IV of the Environmental Protection Act; and 4) the tangible personal property being purchased will be used in the construction or maintenance of the community water supply operated by the not-for-profit corporation.

In order for the construction contractor to obtain the benefit of the exemption on purchases of tangible personal property purchased from suppliers on behalf of a not-for-profit corporation that

qualifies for the exemption, the construction contractor should certify to the supplier that the tangible personal property being purchased will be used in the construction or maintenance of the community water supply operated by the not-for-profit corporation and provide the supplier with a copy of the certificate obtained from the not-for-profit corporation to document the exemption. The supplier should maintain these certifications in its books and records.

Please be advised that the Department plans on filing a proposed rulemaking concerning the exemption in the near future. You may want to monitor the Department's website for information regarding the proposed rulemaking.

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Richard S. Wolters
Associate Counsel

RSW:msk